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SENSITIVE
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STATE FOR EAP/MTS AND EEB/IFD/OFD - STATE PASS TO WORLD BANK US
EXECUTIVE DIRECTOR

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SUBJECT: TIMOR-LESTE SEEKS WORLD BANK CONTRITION

Summary

¶1. Timor-Leste Minister of Finance Pires called in the Ambassador on May 21, 2009, to ask for U.S. support to resolve a dispute with the World Bank. The conflict concerns a financial management technical assistance project that is both a flagship program for the World Bank in Timor-Leste, and a key element of the Finance Minister's effort to modernize and reform the Timorese government's financial management, accountability and effectiveness. World Bank headquarters may have behaved badly and needlessly by in effect publicly scolding the Timorese without prior consultation and in the midst of a highly politicized debate in Dili. The program in question is not without its blemishes: its consultants receive eye-popping salaries by Timorese standards and an ongoing review may reveal inappropriate political influence over employment decisions. Nevertheless, especially given the important advisory role the Bank provides in fiscal policy, we recommend at minimum that the Bank's leadership send a senior mission to Timor-Leste to better explain its actions. End summary.

¶2. (SBU) A major domestic challenge facing the government of Prime Minister Gusmao virtually from the day it took office in 2007 has been the persistent accusation of corruption made by the leading opposition party, Fretilin, and others. The nature of the allegations has evolved over time, but Fretilin's consistent drumbeat has been that the current government is misusing and misappropriating Timor-Leste's scarce financial resources. The Prime Minister, in turn, has periodically and sharply riposted that corruption was far worse and more prevalent during the Fretilin-led governments of 2002-07. An earlier fracas centered on subsidized imports of rice, with the government and Fretilin trading brickbats over which was more wasteful or fraudulent when importing one of Timor-Leste's staple foods. The most recent dispute has been over a key World Bank technical assistance program in Timor-Leste, the Planning and Financial Management Capacity Building Program (PFMCBP).

¶3. (SBU) The PFMCBP supports the Ministry of Finance, its agencies, line ministries, and district entities involved in financial management. It aims to strengthen planning, budgeting, public expenditure management, and revenue administration with emphasis on efficiency, effectiveness,

accountability, integrity, service culture, and transparency. For all practical purposes, it is the only systematic effort currently underway to help the Government of Timor-Leste improve the management of its state finances. Australia, New Zealand, Norway, Ireland, and the European Union are major donors. Although the U.S. has considered contributing to the program, we have no current financial stake. As a potential donor, both the World Bank and the Finance Ministry has been in contact with the embassy and USAID regarding the ongoing dispute.

¶4. (SBU) Timorese public attention has been drawn to the salaries PFMCBP consultants are receiving. An intrepid Timorese journalist broke the story several weeks ago and posted online the full recruitment and benefit dossiers of more than eighty World Bank consultants assigned to the Finance Ministry's project. The remuneration being received by some World Bank consultants was eye popping - over \$500,000 annually in a country where more than half the population survives on less than \$0.88 a day. Timorese attention also focused on the cases of three Timorese nationals employed in the program thought to be under-qualified, politically close to the Finance Minister and earning far, far in excess of regular Timorese civil servants. One such Timorese reportedly is drawing an annual stipend of \$200,000, while public servant salaries here typically hover around several hundred dollars per month. The opposition party Fretilin accused the government of a variety of sins, including corruption, nepotism and lavishing large sums on low quality advisors. The cases generated sufficient public outcry that members of a party within the ruling coalition joined Fretilin in demanding that the finance minister appear before parliament to explain.

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¶5. (SBU) The Prime Minister held an extraordinary press conference on May 13 to support the government and the World Bank program. He stoutly defended the practice of using foreign advisors as essential to improving the qualitative operations of the government and, in a deliberate bid to insulate the World Bank from criticism, described their salaries as determined by the international market. The PM also asserted that not only did corruption occur more frequently under the old Fretilin government, but so did the practice of hiring expensive foreign advisors (indeed, the PFMCBP was begun by the Fretilin government, although substantially overhauled by the current finance minister). In the middle of this domestic dispute, and after the Prime Minister's public defense of both the program and the World Bank, the latter released a press statement on May 14. Although carefully worded (it is available on the bank's website), it states the World Bank is reviewing contracts made between the Timorese government and consultants, notes concern about the level and cost of international technical assistance, suggests the PFMCBP has been too costly, and asserts the bank has raised the need to reduce the number of consultants with the Timorese government. It is viewed, by both the Prime and Finance Ministers, as unfriendly, damaging and disloyal. On May 15, the prime minister instructed his government to halt all contact with World Bank staff.

¶6. (SBU) Finance Minister Pires on May 21 told the Ambassador that she views the PFMPCB as core to her effort to reform her ministry's - and eventually the full government's - financial management and raise its ability to execute public programs. She described the controversial Timorese consultants as communications experts essential to her ability to convince Timorese stakeholders of the need for payments reform, as well as securing their acceptance of new disciplines. She emphasized the Prime Minister's effort to insulate the World Bank from the domestic controversy, decried the reference in the Bank's statement to an ongoing review of the PFMCBP (the review had

been agreed to a year ago), described the Bank's actions as a "betrayal" and an effort to "wash its hands" of a program in which, before May 14, it had been a full, uncomplaining and active partner.

17. (SBU) The Finance Minister reported that she sent the World Bank president a letter asking the Bank to "undo the damage." She asked the ambassador for U.S. support in convincing the Bank's leadership that it must make an effort to fix the current situation, including offering an apology to Prime Minister Gusmao. She summarized her view of the World Bank's May 14 actions as "disrespectful," symbolic of the inherent imbalance in the relationship between an enormous international institution and a small nation such as Timor-Leste. She also urged the U.S. to work to improve communications between the Bank and its office in the Dili (the local World Bank staff reportedly argued against the May 14 press release, but their concerns were overruled by headquarters).

Comment

18. (SBU) On May 17, Prime Minister Gusmao told the Ambassador in regard to the dispute with the World Bank that, "since 1999, we've done everything they've asked us to do; now, when we need their help, they run away - it's unfair." The PFMCBP is not without blemishes. So far, it has added more international capacity than it has built Timorese skills. And the ongoing review may well reveal poor hiring decisions including by the Finance Minister. That said, a long-lasting rift with the World Bank would be harmful to U.S. goals in Timor-Leste as the Bank provides services, especially macroeconomic and fiscal policy advice, that no other donor has the resources or expertise on the ground to replace (especially with the imminent closure of the IMF representative office in Dili). Nobody is more aware of the potential damage of a rupture with the Bank than the

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Timorese government. Although the no-contact policy is formally in place, the Prime and Finance Ministers have reached out to both Washington and local Bank staff. That said, the Bank's decision to release the May 14 statement without prior consultation with the Timorese leadership or clearance from major donors to the PFMCBP (Australia in particular is bruised on this point) appears to us as ill-conceived and, frankly, inexplicable. Mission Dili requests the Departments of State and Treasury, through the U.S. Executive Director's Office at the World Bank, to encourage the World Bank to dispatch a senior official to Dili to explain its actions, apologize if necessary, and repair relations with the government of Timor-Leste.

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